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July 24, 2014

The Honorable Thomas E. Perez  
Secretary  
United States Department of Labor  
200 Constitution Avenue, NW  
Washington, DC 20210

Dear Mr. Secretary:

Thank you for the opportunity to share with you the California Public Employees' Retirement System's (CalPERS) implementation of the out-of-pocket limitations contained in the Affordable Care Act (ACA) with respect to CalPERS' use of reference-based pricing.<sup>1</sup> Since its passage in 2010, CalPERS has been an ardent supporter of the ACA, with its promise to expand health care access to millions of Americans, promote quality care, and control costs.

As an active health benefits purchaser, CalPERS is a prime example proving that a well-designed reference pricing program can work in both the favor of the member and the purchaser to drive down health care costs while maintaining or improving quality and access. Reference pricing is an integral part CalPERS value-based purchasing design strategy and provides an additional mechanism to help keep our members' plans more affordable.

CalPERS is the largest public employer health benefits purchaser in California and the second largest employer purchaser in the nation after the federal government. We provide health benefits to approximately 1.4 million active and retired state, local government, and school employees and their family members. Our health plan offerings include health maintenance organization (HMO), self-funded preferred provider organization (PPO), and exclusive provider organization plans. In 2013, CalPERS spent more than \$7.5 billion to provide health benefits to our members.

### Background

Several years ago, to better understand the health status of CalPERS' membership and to identify opportunities to reduce unwarranted variability in cost, quality, and health care utilization, CalPERS began an effort to identify members with the highest risk and cost conditions, assess cost and utilization compared to regional norms, and profile specific conditions. Based on this analysis, CalPERS determined osteoarthritis was our number

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<sup>1</sup> FAQs about Affordable Care Act Implementation, Part XIX, Question 4. Available from: <http://www.dol.gov/ebsa/faqs/faq-aca19.html>

one cost driver.<sup>2,3</sup> As such, we asked Anthem Blue Cross (Anthem), our third-party administrator for our PPO plan offerings, to examine high cost osteoarthritis procedures and identify the potential for a value-based purchasing design program.

In 2011, CalPERS introduced the concept of reference pricing into our benefit design. We established a \$30,000 payment threshold for routine, elective single knee and hip joint replacement surgery in each of our three PPO plans. The \$30,000 threshold is the maximum for the in-patient hospital stay and device; it does not include the surgeon's fee or other physicians involved in the patient's care. The threshold limits the financial obligation of our plans and guarantees CalPERS' members in those plans the ability to choose among over 50 quality facilities throughout the state, including Stanford Hospital and Cedars-Sinai Medical Center, that provide services within what we believe is an appropriate cost range and with no additional financial exposure other than the member's existing deductible, co-payment and co-insurance. The dollar amounts associated with these items comply with the ACA's cost-sharing requirements.

Members may still choose a facility that does not participate in reference pricing, but would be responsible for the deductible, co-payment and co-insurance, all of which are applied toward the member's annual out-of-pocket maximum as required by the ACA, as well as any charges above the \$30,000 reference price, which are not applied toward the member's annual out-of-pocket maximum. Note that if a CalPERS member chooses a hospital that does not participate in reference pricing, and if that hospital's price is below the threshold, he or she will not incur additional charges beyond the standard out-of-pocket costs. One result of the program is that it has helped make health care prices more transparent to our members and encouraged them to select more efficient, lower cost facilities.<sup>4</sup> Pricing transparency is important so that members can determine how their out-of-pocket costs may vary among hospitals.<sup>5</sup>

In 2012, CalPERS extended reference pricing to colonoscopies, cataract surgery, and arthroscopy procedures conducted in outpatient facilities. CalPERS is currently in the evaluation phase of these procedures.

### Program Design Considerations

The U.S. Department of Labor and other federal agencies charged with implementing the ACA may wish to consider the following components, based on CalPERS' reference pricing program experience. We believe these components balance the competing priorities of preserving medical management to control costs, limiting member financial exposure, and maintaining member access to medically-appropriate, quality care.

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<sup>2</sup> Muscle/Bone Disorders: Health Care Decision Support System Reporting Program. CalPERS Health Benefits Committee Agenda Item 4c. September 15, 2009.

<sup>3</sup> Population Health Study-Part II. CalPERS Health Benefits Committee, Agenda Item 3a. February 17, 2010.

<sup>4</sup> CalPERS Supports Health Care Pricing Transparency Initiative (press release). November 2, 2012. Available from: <http://www.calpers.ca.gov/index.jsp?bc=/about/newsroom/news/2012/health-care-pricing.xml>.

<sup>5</sup> Amanda E. Lechner, Rebecca Gourevitch, Paul B. Ginsburg. The Potential of Reference Pricing to Generate Health Care Savings: Lessons from a California Pioneer. Center for Studying Health System Change. HSC Research Brief No. 30. December 2013. Available from: <http://www.hschange.org/CONTENT/1397/>

## 1) *Focus on Quality*

From the beginning, CalPERS focused on ensuring that members participating in reference pricing had access to quality facilities. One of our quality requirements was that the designated facility met procedure volume thresholds, quantified as the facility performing at least 10 joint replacements for CalPERS' members in each surgery category in the previous 18 months. In addition, Anthem examined surgical infection prevention data submitted to the Joint Commission, as well as its proprietary hospital performance scoring, to ensure facilities maintained high-quality standards.<sup>6</sup> In a study after the implementation of the program, our members who had surgery at a designated facility had significantly lower general complication and general infection rates, and similar follow-up admission rates, in comparison to non-CalPERS members enrolled in plans offered or administered by Anthem receiving treatment at a non-designated facility.<sup>7,8</sup> Additionally, HealthCore, a research arm of Wellpoint, Anthem's parent company, recently completed a follow-up survey with CalPERS' members who have had surgery at a reference pricing facility. The survey's preliminary results are positive and consistent with the post-surgery outcomes results. The results of this survey will be released in the future.

## 2) *Focus on Access*

A reference pricing program should be structured to maintain access to a broad provider network. CalPERS ensured that our members had access to a sufficient number of hospital networks in which to obtain the hip or knee procedure. Working with Anthem, we established that 46 facilities across California met our quality, access, and pricing standards; that number has now increased to 53. CalPERS and Anthem factored in the geographic distribution of designated facilities so that, in most cases, members would not have to travel more than 50 miles from their home for surgery. If a facility is not available within the member's area, CalPERS provides a travel benefit (transportation and lodging) for the member and a companion. In addition, medical exceptions are made for non-routine procedures. After beginning our reference pricing program, several non-designated hospitals renegotiated their contracts with Anthem to become designated hospitals for all individuals enrolled in a plan offered or administered by Anthem, not just CalPERS' members, thereby expanding access and making the procedures more affordable for more Californians.<sup>9</sup>

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<sup>6</sup> U.S. Department of Health and Human Services, Agency for Healthcare Research and Quality. Reference-Pricing Policy for Hip/Knee Replacements Generates Significant Savings by Encouraging Enrollees To Choose High-Value Facilities. May 21, 2014. Available from: <http://www.innovations.ahrq.gov/content.aspx?id=4069>.

<sup>7</sup> WellPoint (Press Release). CalPERS Members Had Similar to Better Outcomes at Facilities Charging Less for Hip and Knee Replacements. Available from: <http://ir.wellpoint.com/phoenix.zhtml?c=130104&p=irol-newsArticle&ID=1832119&highlight>.

<sup>8</sup> Chia-hsuan Li. Effects of a Reference-Based Purchasing Design Program on Healthcare Utilization and Outcomes of Knee and Hip Replacement Surgeries. HealthCore, Inc. Presentation before AcademyHealth Annual Research Meeting, Baltimore, MD. June 23, 2013. Available from: <http://www.academyhealth.org/files/ARM/2013/All%20Podium%20Presentations.pdf>

<sup>9</sup> Amanda E. Lechner, Rebecca Gourevitch, Paul B. Ginsburg. The Potential of Reference Pricing to Generate Health Care Savings: Lessons from a California Pioneer. Center for Studying Health System Change. HSC Research Brief No. 30. December 2013. Available from: <http://www.hschange.org/CONTENT/1397/>.

### 3) *Targeted Member Education and Engagement*

CalPERS and Anthem employed multiple communication methods to outreach to and inform members about reference pricing. We mailed announcements about reference pricing to our PPO membership, provided information in our open enrollment and evidence of coverage materials, discussed the program in constituent meetings, notified all orthopedists, primary care physicians, and hospitals in Anthem's network about the program by mail, and sent letters to members who had seen an orthopedic surgeon in the past year for hip or knee conditions. The mailings included a list of designated facilities and map with their locations throughout the state. Anthem's website for CalPERS' members also includes information about our reference pricing program, including member tools to identify low cost providers by procedure through "Anthem Care Comparison." In addition, prior to an elective hip or knee surgery, members must be pre-approved. Once approved, Anthem sends a pre-certification letter that explains reference pricing and the member's financial responsibilities.

### 4) *Use Data to Drive Decision Making*

Anthem analyzed its cost and quality data and found significant variation in hospital pricing throughout California for hip and knee replacements, ranging from \$15,000 to \$110,000, with no correlation between price and quality.<sup>10,11</sup> CalPERS, in our earlier population health study, also found wide geographic and treatment cost variation for osteoarthritis throughout the state.<sup>12</sup> Based on claims data analysis, Anthem determined that \$30,000 would be an appropriate upper payment limit for elective hip and knee replacements, while still providing savings to CalPERS.<sup>13</sup> At the time the price was set, approximately two-thirds of California hospitals performing hip and knee surgeries on Anthem patients charged less than \$30,000.<sup>14</sup> In the first two years of the program, researchers at the University of California at Berkeley estimate cumulative savings of \$5.5 million, with the average hip or knee replacement charge declining by 26 percent, or an average of \$9,000 per procedure.<sup>15,16</sup>

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<sup>10</sup> WellPoint (Press Release). CalPERS Members Had Similar to Better Outcomes at Facilities Charging Less for Hip and Knee Replacements. Available from: <http://ir.wellpoint.com/phoenix.zhtml?c=130104&p=irol-newsArticle&ID=1832119&highlight>.

<sup>11</sup> U.S. Department of Health and Human Services, Agency for Healthcare Research and Quality. Reference-Pricing Policy for Hip/Knee Replacements Generates Significant Savings by Encouraging Enrollees To Choose High-Value Facilities. May 21, 2014. Available from: <http://www.innovations.ahrq.gov/content.aspx?id=4069>.

<sup>12</sup> Population Health Study-Part II. CalPERS Health Benefits Committee, Agenda Item 3a. February 17, 2010.

<sup>13</sup> Amanda E. Lechner, Rebecca Gourevitch, Paul B. Ginsburg. The Potential of Reference Pricing to Generate Health Care Savings: Lessons from a California Pioneer. Center for Studying Health System Change. HSC Research Brief No. 30. December 2013. Available from: <http://www.hschange.org/CONTENT/1397/>

<sup>14</sup> Payers Test Reference Pricing And Centers of Excellence To Steer Patients To Low-Price And High Quality Providers. James Robinson, Kimberly MacPherson. September 2012. Vol. 31, no. 9, p. 2028-2036.

<sup>15</sup> Hips and Knees Reference Based Pricing Evaluation. CalPERS Pension & Health Benefits Committee Agenda Item 7. June 18, 2013. Available from: <http://www.calpers.ca.gov/eip-docs/about/committee-meetings/agendas/pension/201306/item-7.pdf>.

<sup>16</sup> U.S. Department of Health and Human Services, Agency for Healthcare Research and Quality. Reference-Pricing Policy for Hip/Knee Replacements Generates Significant Savings by Encouraging Enrollees To Choose High-Value Facilities. May 21, 2014. Available from: <http://www.innovations.ahrq.gov/content.aspx?id=4069>.

## 5) *Best Practices*

CalPERS found that reference pricing is most appropriate for elective, nonemergency procedures and surgeries that the member can schedule in advance. In addition, reference pricing is especially appropriate when there are large price variations within regions without a difference in quality. Another consideration is that reference pricing works best for procedures that are relatively straightforward, without much variation in the diagnosis or treatment method.<sup>17</sup>

### Conclusion

We believe reference pricing is consistent with the intent of the ACA, while preserving a reasonable degree of cost control to help make health care more affordable for our members. CalPERS' reference pricing program ensures access to high-quality, medically appropriate care, as evidenced by the data that supports our benefit design. CalPERS believes reference pricing promotes access to, and use of, higher value providers, treatments, and services as well as fosters equal or better quality and efficiency by encouraging individuals to use lower cost treatment settings.

CalPERS is committed to being a collaborative partner to help ensure the successful implementation of the ACA. Please contact me at [ann.boynton@calpers.ca.gov](mailto:ann.boynton@calpers.ca.gov), or 916-795-0404, if you have any questions or wish to discuss these issues further.

Regards,



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<sup>17</sup> U.S. Department of Health and Human Services, Agency for Healthcare Research and Quality. Reference-Pricing Policy for Hip/Knee Replacements Generates Significant Savings by Encouraging Enrollees To Choose High-Value Facilities. May 21, 2014. Available from: <http://www.innovations.ahrq.gov/content.aspx?id=4069>.